

BEFORE THE STATE BOARD OF EQUALIZATION  
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of )  
FRED B. NEUHOFF COMPANY )

Appearances:

For Appellant: Fred B. Neuhoﬀ, President of said  
corporation

For Respondent: Albert A. Manship, Franchise Tax Commis-  
sioner

O P I N I O N

This is an appeal pursuant to Section 25 of the Bank and Corporation Franchise Tax Act (Chapter 13, Statutes of 1929) from the action of the Franchise Tax Commissioner in ruling adversely upon the protest of Fred B. Neuhoﬀ Company to his proposed assessment of an additional tax of \$342.70, based upon the return of the corporation for the year ended February 28, 1930. The sole point presented on the appeal is whether or not the Commissioner is justified in refusing to allow a loss claimed by the Appellant from the sale of certain real property acquired prior to January 1, 1928, and sold during the fiscal year covered by its return above mentioned.

No evidence has been presented as to the value of the property in question on January 1, 1928, and the position of the Commissioner is that he had no alternative but to disallow the claimed loss and assume that the property was worth no more then than when it was sold a short time afterwards. However, the taxpayer refers to decisions of the United States Supreme Court holding that in the administration of the federal income tax, March 1, 1913 values could not be used where there had been no gain over the original capital invested (Goodrich v. Edwards, 255 U. S. 527; Walsh v. Brewster, 255 U. S. 536). Since March 1, 1913 was the basic date for the federal law, by analogy the same principle is said to be applicable to the California Act.

The pertinent provisions of the law are as follows:

"For the purpose of ascertaining the gain derived or loss sustained\* \* \* in the case of property acquired prior to January 1, 1928, and disposed of thereafter, the basis shall be the fair market value thereof as of said date."  
(Section 19, Chapter 13, Statutes of 1929)

The Federal Revenue Act of 1916 contained a provision

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corresponding to Section 19 of the Act above quoted to the effect that the basis for the determination of gain or loss of property acquired before March 1, 1913, was "the fair market price or value of such property as of March first, nineteen hundred and thirteen."

This provision was considered by the United States Supreme Court in the case of Goodrich v. Edwards, 255 U. S. 527, which has been cited by the Appellant. In that case the taxpayer acquired property, in 1912, having a value of \$291,600. On March 1, 1913, the value of the property was \$148,635.50. It was sold in 1916 for \$269,346.25, obviously at a loss to the owner. The Court held that although the selling price was greater than the value of the property on March 1, 1913, there was no taxable gain because there had been no actual income from the transaction.

A somewhat similar problem was considered in the case of United States v. Flannery, 268 U. S. 98, involving the interpretation of the basic date clause in the 1918 Federal Revenue Act which was substantially the same as that in the 1916 Act already quoted. Prior to March 1, 1913, James Flannery had bought certain corporate stock for less than \$95,175. On the basic date its value was \$116,325, but he sold it in 1919 for \$95,175. The question arose as to whether or not he had suffered a loss in the year 1919 representing the difference between the sale price and the March 1, 1913 value. The Supreme Court upheld the Commissioner of Internal Revenue in disallowing the claimed loss saying:

"It is clear, in the first place, that the provisions of the Act in reference to the gain derived and the losses sustained from the sale of property acquired before March 1, 1913, were correlative, and whatever effect was intended to be given to the market value of property on that date in determining taxable gains, a corresponding effect was intended to be given to such market value in determining deductible losses."

After referring to the cases of Goodrich v. Edwards and Walsh v. Brewster already mentioned, the Court continued:

"So we think it should be held that the Act of 1918 imposed a tax and allowed a deduction to the extent only that an actual gain was derived or an actual loss sustained from the investment, and the provision in reference to the market value on March 1, 1913, was applicable only where there was such an actual gain or loss, that is, that this provision was merely a limitation upon the amount of actual gain or loss that would otherwise have been taxable or deductible."

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From these cases we deduce the proposition that if there is a gain after the basic date it will be taxable only to the extent that it represents an actual gain over the whole transaction. Correspondingly, if there is a loss after the basic date, that portion thereof which represents an actual loss from the whole transaction will be deductible. It must be borne in mind, however, that these cases are interpreting an income tax while the statute under which this appeal is taken imposes a tax "according to or measured by" net income. On occasion the Courts have recognized a marked distinction between the two types of taxation (Flint v. Stone Tracy Co., 220 U. S. 107; Educational Films Corporation of America v. Ward, 51 Sup. Ct. Rep. 170). A literal reading of the provisions of Section 19 of the Act seems to call for the conclusion that the January 1, 1928 value of the property sold must be used as the basis of determining the gain derived or the loss sustained. For the reasons indicated, this may be unconstitutional if interpreted literally but due to the differences existing between the nature of the federal tax and the nature of the state tax, the United States Supreme Court decisions are not directly in point and we feel constrained to hold that the law must be given a literal interpretation notwithstanding the apparent injustice which may result in some cases.

At least, so far as the present case is concerned, we are unable to say whether any loss has been sustained since January 1, 1928, because we have been afforded no evidence of the value of that date. Consequently, we conclude that the Appellant has made no showing that he is entitled to relief from the action of the Commissioner in disallowing the loss claimed because the sale price of the property in 1929 was \$10,034.59 less than the cost prior to January 1, 1928.

O R D E R

Pursuant to the views expressed in the opinion of the Board on file in this proceeding and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, that the action of the Franchise Tax Commissioner in overruling the protest of Fred B. Neuhoﬀ Company, a corporation, against a proposed assessment of an additional tax in the amount of \$342.70, based upon the return of said corporation for the year ended February 28, 1930, under Chapter 13, Statutes of 1929, be and the same is hereby sustained.

Done at Sacramento, California, this 14th day of December, 1931, by the State Board of Equalization.

Jno. C. Corbett, Chairman  
R. E. Collins, Member  
Fred E. Stewart, Member  
H. G. Cattell, Member

ATTEST: Dixwell L. Pierce, Secretary